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# Minutes

## Board of Natural Resources Meeting

November 7, 2006  
Natural Resources Building, Olympia, Washington

### BOARD MEMBERS PRESENT

Daniel J. Bernardo, Dean, Washington State University, College of Agricultural, Human, and Natural Resource Sciences

Terry Bergeson, Superintendent of Public Instruction

Doug Sutherland, Commissioner of Public Lands

Bob Nichols, for Governor Christine Gregoire

Bruce Bare, Dean, University of Washington, College of Forest Resources

### BOARD MEMBERS ABSENT

Ted Anderson, Commissioner, Skagit County

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### CALL TO ORDER

Chair Sutherland called the meeting to order at 9:05 a.m. on, November 7, 2006, in Room 172 of the Natural Resources Building.

### APPROVAL OF MINUTES

MOTION: Terry Bergeson moved to approve the October 3, 2006 Board of Natural Resources Meeting Minutes.

SECOND: Bruce Bare seconded.

ACTION: Motion passed unanimously.

### PUBLIC COMMENTS FOR AGENDA ACTION ITEMS

Bill Robinson - Nature Conservancy

Mr. Robinson came forward to comment on the Trust Land Transfer Program stating that it's a great program that benefits all parties.

### LAND TRANSACTIONS

SAM & SAM's Neighbor #08-078863 (Handout1)

Julie Armbruster came forward to present. She began by stating that the SAM Purchase proposal would acquire two parcels known as SAM and SAM's Neighbor, both developed mixed fruit orchards, for sale by Stemilt Associates. The property is located south of Mattawa in Grant County. She explained that the two parcels total 713.5 acres and are currently owned by Stemilt Associates and Thomas and Lorraine Mathison. The property is managed by Stemilt Management Inc. and they will become the lessee to the State at closing. River water for irrigation is from three certificates owned by Green Acres Orchards, a partnership of area landowners. DNR would acquire the shares owned by the sellers.

Ms. Armbruster gave the description of the property and revenues stating that the orchard includes several varieties of apples, cherries, plums, and peaches planted on 668.3 acres. The estimated return on the property is 9%, with DNR's share expected to average \$700,000 per year; 3% return is guaranteed by cash rent. The purchase price is \$7,750,000 to be purchased with Land Bank and Real Property Replacement Account funds.

She informed the Board of the benefits saying that the Common School Trust would acquire developed, productive agriculture property that is leased by a company known for its high quality operations. The trust would begin receiving revenue in the 2007 crop year.

MOTION: Terry Bergeson moved to approve resolution 1214.

SECOND: Dan Bernardo seconded.

DISCUSSION: Board members discussed the orchard and Ms. Armbruster informed them that the plantings are a various mix of old and new with an emphasis on phasing out the old.

ACTION: Motion passed unanimously.

#### 2007-2009 TLT Proposal for Legislative Consideration (Handout2)

Mr. Challstedt came forward to present. He began by discussing the 2007-2009 Trust Land Transfer Proposal.

He stated that the program goals are to provide immediate revenue for schools with the timber value funding schools directly and the land value funding schools indirectly. The trust would divest of lands that have special ecological and/or social attributes. The Trust would reinvest in revenue productive properties such as: commercial forest land, commercial agricultural land, and commercial real estate. Special properties would be protected for public benefit.

He explained that the program uses funds appropriated for K-12 education to provide immediate revenue for schools, future revenue for schools, and protection for special lands.

He then discussed the Trust Land Transfer Program Diagram stating that legislative funds serve a dual purpose of providing revenue for school construction and acquiring special properties for public benefit. The legislative appropriation proposal for the 07-09 biennium is \$100,000,000.

Mr. Challstedt went on to discuss the 07-09 proposal:

#### Requested Legislation

- Appropriation request
  - o Transfers (33 properties): \$100,000,000
  - o Replacement purchases: \$19,000,000
- Five properties with high land value to be transferred by lease

#### Transfer Conditions

- Minerals to be reserved
- Deed restriction for designated use
- Habitat Conservation Plan (HCP) to be retained on critical habitat lands

#### Process Time Line:

11/06: DNR submits proposal for Board of Natural Resources (BNR) review

04/07: Legislature approves budget bill with TLT appropriation, direction, and property list  
07/07: DNR begins implementation, appraisals are initiated, projects presented for BNR approval  
10/08: 2009-11 TLT list presented to BNR  
06/09 2007-09 TLT transfer complete, remaining funds transferred to the school account

He then listed the TLT recipients:

- DNR NAP/NRCA
- State Parks and Recreation Commission
- Department of Transportation
- Department of Fish and Wildlife
- Eight Counties
  - o Clark, Island, Jefferson, King, Pend Oreille, Pierce, San Juan, Spokane
- Key Peninsula Metropolitan Park District
- Peninsula Metropolitan Park District
- City of Tacoma

Chair Sutherland asked for concurrence on the submittal of the 2007-09 TLT Program.

MOTION: Terry Bergeson moved to submit the list to the legislature for the TLT Program.

SECOND: Bruce Bare seconded.

ACTION: Motion passed unanimously.

#### Far Out North TLT #02-077614 (Handout2)

Mr. Challstedt presented. He stated that the Far Out North parcel is located in King County, 10 miles west of I-90 at Easton. It is located within the Tacoma Green River Watershed and is to be transferred to Tacoma Public Utilities. The parcel is comprised of 339 acres of Common School Trust with a total value of \$4,887,000. The benefits are that the Trust divests of low-income producing property, timber value benefits school construction, land value is reinvested in productive land, and the DNR HCP will be retained on the land.

MOTION: Terry Bergeson moved to approve resolution 1215.

SECOND: Bob Nichols seconded.

ACTION: Motion passed unanimously.

### **TIMBER SALES (Action Item)**

#### Proposed Timber Sales for December 2006 (Handout 3)

Jon Tweedale came forward to present. He began by discussing the Tripod Complex Fire. He stated that 4,800 acres of timber burned and about 10-15 MMBF of timber is salvageable. Four sales have already been sold equaling 1.1 MMBF. There are an additional six sales equaling 10.4 MMBF with a completion date of sale by June 2007.

He then discussed Bisbee Mountain-Kettle Falls saying that 2.4 MMBF equaling 200 acres would be sold by the first quarter of 2007.

Mr. Bare asked where this wood was going.

Mr. Tweedale said the wood is going everywhere and there's a lot of interest.

Mr. Tweedale stated that although lumber prices are softening, log and stumpage remain strong. One economist suggests their forecast COST floor for minimum operating rates were too high with manufactures still willing and able to pay higher log and stumpage prices.

October 2006 Sales Results:

9 sales offered & 9 sold; 27.2 mmbf offered & 27.2 mmbf sold; \$7.6 million minimum bid & \$9.3 million sold; \$279/mbf offered & \$342/mbf sold; average number of bidders = 3.7; 22% above minimum bid.

Proposed December 2006 Board Sales:

13 sales at 56.3 mmbf, \$15.5 million minimum bid with an average of \$276/mbf. All sales are SFI Certified.

MOTION: Terry Bergeson moved to approve the December 2006 timber sales.

SECOND: Bruce Bare seconded.

ACTION: Motion passed unanimously.

## CHAIR REPORTS

### Bellingham Harbor Line Proposal

Rich Doenges presented. He began by discussing the Harbor Line Relocation Procedure which included a completed application, public outreach and consultation, evaluation, staff recommendation, and finally a Harbor Line Commission Decision.

He explained the Port of Bellingham Proposal as such: To relocate inner and outer harbor lines at the City of Bellingham's Waterfront and the Fairhaven Port Management Area. The authority comes from Article XV of State Constitution RCW 79.115.020 and WAC 332-30-116. The Harbor Line Commission maintains the capability of harbor areas for commerce and navigation purposes.

Mr. Doenges then detailed a brief timeline saying that August 15, 2006 there was a workshop including a presentation of the Port's proposal. October 10, 2006 there was an informational meeting including a presentation of options. November 14, 2006 there is a scheduled formal public hearing. He then discussed the options:

- Eight geographical sub areas bay wide were developed based on shoreline uses
- Three options presented for each sub area
  - o Relocation of harbor lines
  - o Removal of the harbor lines
  - o No change of the harbor lines

He then briefed the Board on aspects considered in DNR's final recommendation:

- Long-term needs of water dependent commerce and adequate space for navigation
- Plans of public ports, counties, cities, and other local, state and federal agencies
- Economic, environmental, and cumulative impacts
- Public access to waterfront
- Indian treaty rights
- Precedent setting effect on other harbor areas

Mr. Doenges concluded by stating that the deadline for SEPA comments is Monday, November 20, 2006, and that the proposed Harbor Line Commission Action is scheduled for Tuesday, January 2, 2007.

#### Asset Management Briefing

Bonnie Bunning came forward to introduce the Asset Management Briefing.

Clay Sprague began by discussing Asset Management Past, Present, and Future. He stated that today he would be providing an historical overview of the trust land endowment, land transaction authorities, and legislative intent in granting these authorities.

He talked about the focus on department asset repositioning strategies up till now and the impact of those strategies on the land base; he also discussed looking toward the future.

He stated that as with most western States, the State of Washington received its original grant of trust lands at statehood. The Enabling Act of 1889 granted to the State of Washington sections 16 and 36 of every township for the support of common schools as well as other lands to support a variety of other public institutions. Where these sections were not available due to sale or reservation by Congress, the state was given the authority to select other federal lands in lieu of these lands. These in lieu selections which began immediately were really the first land transactions taken to improve the position of the land base on behalf of the trusts. These in-lieu selections weren't actually completed until the early 1980's. Some states are still struggling to complete their selections.

Mr. Sprague pointed out a table on the presentation that showed the collective federal grant land endowment at just over 3.1 million acres. The purpose of the lands is to manage them to support common schools and other public facilities.

He stated that the next major addition to Washington's trust land base occurred in the 1920's and 30's. The Legislature established a state forest land system by authorizing the state purchase of logged-over forest land, acceptance of gifted properties, and county-deeded lands, which

- chiefly had value for developing and growing timber,
- are of sufficient acreage and so located that it can be economically administered for forest development purposes

Mr. Sprague said those lands are to be professionally managed by the state as state forest trust lands (formerly known as state forest board lands) with the proceeds going to the county and junior taxing districts in which the lands are located. This has added over 600,000 acres to the trust land base.

Over time, over 3.7 million acres made up the trust land endowment.

He discussed the early history of trust lands pointing out that it includes a period of rapid disposal of trust lands to fund schools. When this occurred it generated concern in Congress and the states over the loss of lasting benefits for the schools.

Provisions in the Washington's Constitution directed that school lands cannot be sold for less than fair market value and no more than 160 acres could be sold at a time; with restriction that no more than ¼ of the lands could be sold before January 1, 1895, and no more than half before January 1, 1905.

Mr. Sprague stated that these restrictions were a reaction to a growing desire in the late 19<sup>th</sup> century, of congress and the states, to move from a policy of rapid disposal of state trust lands to one of retention and long-term management.

He said that although that was the case Washington did sell off a portion of its original grant lands throughout the early 1900's.

He continued stating that since statehood, the Washington legislature has granted the Department, through the Board of Natural Resources, the authority to sell, purchase and exchange state trust lands to improve trust land performance in the face of changing circumstances but also to maintain the trust land base for multiple benefits.

Starting in the 1920's and 30's with the creation of the state forest lands, the legislature showed this intent by forever reserving these lands from sale so as to maintain the state forest land base (79.22 RCW) but does authorize the state to exchange state forest lands for real property of equal value for the purpose of consolidating and blocking up state lands or for the purpose of obtaining lands having commercial recreational leasing potential. (79.17 RCW) The legislature also authorized the reconveyance of state forest lands back to the county for public park purposes at the request of the county.

In 1957, the legislature authorized the department to exchange any state land for any land of equal value to:

- Facilitate the marketing of forest products
- Consolidate and block- up state lands
- Acquire lands having commercial recreational leasing potential
- Acquire county-owned lands

In 1987, exchange of difficult to manage urban trust lands for equal value urban property with more income potential was also authorized by the legislature.

However, the legislature also made it clear that this authority could not be used to reduce the publicly owned forest land base.

In 1977, the legislature created the land bank after finding that:

“...it may be desirable for the department to sell state lands which have low potential for natural resource management or low income-generating potential or which, because of geographic location or other factors, are inefficient for the department to manage. However, it is also important to acquire lands to replace those sold so that the publicly owned land base will not be depleted.”

The Legislative goes on to say that the land bank is to be used to acquire lands with natural resource production potential.

Prior to this statute, proceeds from the sale of federal grant trust lands were deposited in the permanent funds and replacement lands were not acquired.

Mr. Sprague informed the Board that in 1980 the legislature (Substitute Senate Bill 3195) authorized the very first transfer of trust land for park purposes with the provision that the value (land and timber) be deposited in the newly created Heart Lake Revolving Fund.

“to be utilized by the department of natural resources for exclusive purpose of acquiring real property as a replacement for the Heart Lake property to maintain the land base of the common school trust lands ... .”

In 1985, the legislature again amended RCW 43.51.270 (House Bill 958) to approve four additional TLT's and created the land replacement account called the Park Land Trust Revolving Fund, where the fair market land value of these land transfers would be deposited and used to acquire replacement land.

Beginning in 1989, appropriations were made by the legislature through budget provisos every biennium except one (95-97) to fund additional trust land transfers. The result is the protection of lands with high recreational, scenic, or ecological values while at the same time, compensating trust beneficiaries for the timber value and providing a mechanism to acquire replacement properties with the land value to improve the economic performance to the beneficiaries and maintain the trust land base in perpetuity for the citizens of Washington.

In 1984, the legislature authorized the department, through amendments to the Land Bank Statute, to dispose of unmanageable trust lands in urban areas and to acquire replacement lands of equal value for income production. This was a very significant change in that it allowed the department to purchase commercial real estate as well as other properties with high income potential to replace the disposal of high value but non income producing urban properties.

In the debate leading up to these legislative changes, there were significant fears that the Department would dispose of productive forest lands to purchase commercial real estate. To address this fear the legislature emphasized in its amendments that it was important to:

- Acquire lands for long-term management, and
- Not reduce the publicly owned forest land base so that the diversity of public uses on the trusts lands will be maintained.

The legislature created the real property replacement account to facilitate transfer of trust land to public agencies or to resolve property trespasses without going to public auction while maintaining the real property asset base of the trusts.

The statute specifically states that:

"The legislature finds that the department has a need to maintain the real property asset base it manages and needs an accounting mechanism to complete transactions without reducing the real property asset base".

The statute goes on to state that "The funds in this account shall be used solely for the acquisition of replacement real property and may be spent only when, and as, authorized by legislative appropriation."

Mr. Sprague said that now that he had reviewed the major transaction authorities provided to the Department and the Board over the years and the legislative intent behind those authorities, he would discuss how the land base had been repositioned to meet that intent.

He said that since statehood, but particularly since the 1960's, the Department has been actively using the authorities granted by the legislature to reposition the trust land base through sales, purchases and exchanges as intended by the legislature.

The first public lands map was published in 1962 and shows the distribution of the federal grant and state forest lands as it was just prior to this significant increase in department land transaction activity.

The first major repositioning strategy was blocking up or consolidating state forest lands. This was a result of the new authority granted by the legislature in 1957 to exchange lands and the fact that there were other forest landowners whose forest lands were intermingled with trust lands.

Throughout the 60's, 70's, and 80's the Department focused on blocking up its forest lands in Western Washington, to reduce management costs and increase revenue for the trust beneficiaries.

Since 1957, when the DNR was created, the state has exchanged about 440,000 acres of the endowment land, and received in return about 480,000 acres from other landowners and managers. 40,000 acres plus.

Mr. Sprague indicated that the Department continues to look for opportunities to create or expand consolidated blocks of state forest land all across the state for economic, ecologic, and social benefits in keeping with the intent of the legislature.

He made note that the second major repositioning strategy of the Department is diversification.

In 1984, with the legislative changes to the Department's land acquisition authorities to facilitate disposal of unmanageable trust lands in urban areas and acquisition of income producing property of equal value, the Department began to look for opportunities to diversify each trusts land asset holdings from strictly natural resource properties to other income producing properties as intended by the legislature; but in keeping with the direction to not reduce the publicly owned forest land base.

Using this authority the Department made its first commercial real estate acquisition in 1985.

In 1988 the Department developed the Transition Lands Program which provided a springboard to re-evaluate the Department's asset management strategies and long-term goals for state trust lands. Even though the Department had first looked at classifying trust assets by land use categories in the late 60's and early 70's, the Department now intensified its efforts to classify lands by asset class.

As a result the Department developed diversification strategies both within and between different asset classes as a way to improve the economic performance of the overall trust land asset base.

In 1995, the Department made its first commercial agriculture purchase as part of this diversification strategy.

As a result of this repositioning activity the amount of land in each trust's land base is much different than it was at statehood.

In quick review the State of Washington started with about 3.7 million acres of endowment land that was reduced primarily through land sales (early 1900's) by close to 900,000 acres.

The repositioning has created state forests such as Tiger Mountain, Capital, Yacolt Burn, Tahuya and the newly created Ahtanum State Forest, to name a few.

The non-income class is those acres that are not producing income for a variety of reasons. This asset class includes acres of high value, highly appreciating urban lands that DNR may be holding until the optimum disposal time, to low value, non-productive range lands. These lands, many of which are original "as is, where is" endowment lands are the focus of DNR's transaction strategies.



A couple of things to note 1) Forest still dominates the trust land asset base; and 2) these lands produced over a quarter of a billion dollars in tax-free revenue to support public institutions, money that would otherwise come out the tax payers pocket.

Mr. Sprague moved on to discuss looking forward and talking about how DNR proposes to track economic performance of each trust's land base, a future vision for state trust lands, and future transaction or repositioning strategies.

Mr. Bare added that rates of return would be beneficial for the Board to review.

Mr. Bernardo noted that current market value is the correct denominator because it's focused on the opportunity cost of the assets which change over time. The appreciation is interesting yet the main focus has to be on the asset value because those trusts can't be sold or moved.

Mr. Sprague said there are some opportunities to capture the appreciation on some parcels but not to the extent a private entity might.

Using the Capitol Grant trust land base as a pilot, (because it was small enough to work with but also fairly diverse) Mr. Sprague listed some details on how the Department plans to track economic performance of each trust's land assets to:

- Inform transaction decisions based on overall land base performance, and
- Better communicate that performance to the Legislature, the Board, Beneficiaries, and stakeholders.

#### Asset Classes:

Asset Value - In tracking the economic performance of each trust's assets it will be important to measure return on asset value. Determining asset value of the land assets has not been easy or cheap to do. The last time all the trust land assets were valued was in 1996 by Deloitte and Touche. While useful at the time, it is now outdated, and it was expensive to do.

As a result the Department is working on a methodology for estimating the asset value of each trust's land base on a continuous and cost-effective basis using county assessor data.

Don Krug, from DNR's Budget office, and Greg Richards, DNR's chief appraiser, are exploring a way to do this in collaboration with the counties. If successful it would allow the Department to more easily and effectively estimate asset value and consequently, return on asset value for each trust's land base.

Once we have a measure of asset value we will be able to show cash return on asset value. Over time we should be able to show appreciation as well so we can show total gross return of cash + appreciation.

Mr. Sprague stated that rapid population growth presents both challenges and opportunities for trust land management. This growth, coupled with global competition, has changed the financial structure of the forest and agriculture industry and the value of land. Capitalizing on land value is leading to conversion and fragmentation of productive natural resource lands.

Without a critical mass of forest and agricultural land to supply the supporting infrastructure, the wealth and health of natural resources is at risk--the same natural resources that make Washington an outstanding place to live, work, and play.

- Retention of working farms and forests throughout the state will be a critical conservation strategy, a viable business strategy for the trust beneficiaries, and provide for multiple public values including support of rural, natural resource based communities
- State trust lands will play a critical and unique role in sustaining this state's forest, agriculture and natural heritage lands and providing revenue to the trust beneficiaries
- A maintained and diversified trust land base is in the long-term interests of the trust and the citizens of Washington as intended by this state's founders and the legislature
- Efforts to preserve Washington's natural resources will require partnerships with other agencies and organizations and will be crucial in retaining working farms and forests

Over the next several decades the Department is considering the following strategies to guide its land transactions and asset management decisions on behalf of trust beneficiaries and the citizens of Washington:

- DNR will continue to reposition or acquire productive forest and agricultural lands to help preserve economically viable working farms and forests
- DNR will maintain and expand its holdings of high-performing irrigated and dry-land agriculture lands
- The Department will continue to use transactions to improve the economic performance of each trust's land base
- The Department will use higher and better use values of trust lands to acquire or protect large forest blocks, agricultural lands and diversify the trust land base, including acquisition of commercial real estate
- DNR will hold a significant set of conservation lands, providing a diversity of public conservation values

These trust lands have played and will continue to play a significant role in shaping the future of Washington. As anticipated and directed by the legislature, the ability to continually evaluate and reposition these lands to meet challenges and take advantage of opportunities will be critical to the next generation of trust beneficiaries and citizens of Washington.

Steve Saunders came forward to discuss the Trust Transactions for the 2005-2007 Biennium.

Objectives:

- Consolidation of East Side forests & shrubbe steppe
- Diversification of asset classes
- Protection & enhancement of assets
- Redistribution of assets into core businesses
  - o Agricultural, Commercial, and Forest

Guidance:

- Asset Management Council

- Independent Review Committee
- Transition Lands Plan
- Asset Management Plan
- Asset Allocation Strategy

Asset Management Council allocation strategy for replacement purchases:

- 2/3 to purchase new agricultural and commercial assets--Allocation: \$31.3 million Spent: \$0.6 million
- 1/3 for asset protection and enhancement of the existing land base--Allocation: \$15.6 million Spent: \$2.8 million

Due to legislative and resource constraints, focus has shifted to exchanges.

- 43 transactions closed in FY 2006
  - o Predominately sales and transfers
  - o Two large exchanges
- Biennial total is expected to be around 75
  - o Trust Land Transfers and some additional sales will be completed
  - o Continuing to pursue major purchase opportunities. Expect two or three to be completed in FY 2007.

Mr. Saunders explained that there are a total of 10,319 acres acquired and there have been 10,817 acres disposed. The gross rate of return on disposals is 0.83%; 8.93% on acquisitions; with a comparison of 8.10%.

He listed the exchanges for the 2005-2007 biennium:

- Central Cascades (high value lands for forest blocks)
- WDFW (leases, shrub steppe for forest blocks)
- South Stevens (facilitated: diversified agricultural and timber)
- North Fork Ahtanum (forest blocks)
- West Ahtanum (forest blocks)
- City Limits (Port Townsend expansion)
- Swift Reservoir (PacifiCorp recreation site)

Mr. Bare asked why the legislature is hesitant to appropriate money that's just sitting there.

Mr. Saunders responded that there are some concerns about what kind of investment analysis is being used. There are also concerns about buying up agricultural lands and a perception by some of competing with the private sector.

## **EXECUTIVE SESSION 12:10-12:35**

### **PUBLIC COMMENTS FOR GENERAL ITEMS OF INTEREST**

No public comments.

Meeting adjourned at 12:36 p.m.

Approved this \_\_\_\_ day of \_\_\_\_\_, 2006

\_\_\_\_\_  
Doug Sutherland, Commissioner of Public Lands

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Bob Nichols for Governor Christine Gregoire

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Bruce Bare, Dean, University of Washington

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Daniel J. Bernardo, Dean, Washington State University

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Terry Bergeson, Superintendent of Public Instruction

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Ted Anderson, Commissioner, Skagit County

Attest:

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Sasha Lange, Board Coordinator